

Silvestre A. Fontes
Thomas J. Rappaport
David H. London
Attorneys for Plaintiff U.S. Securities and Exchange Commission
33 Arch Street, 23rd Floor
Boston, MA 02110
617-573-8991 (Fontes)
617-573-4590 (Fax)
fontess@sec.gov
rappaportt@sec.gov
londond@sec.gov

UNITED STATES DISTRICT COURT
DISTRICT OF NEVADA

SECURITIES AND EXCHANGE
COMMISSION,

Plaintiff,

v.

Case No. CV-S-05-0531-PMP-GWF

EXOTICS.COM, INC., L. REX ANDERSEN,
MARLIN R. BRINSKY, DANIEL G.
CHAPMAN, STEPHEN P. CORSO, JR.,
BARRY F. DUGGAN, JAMES L.
ERICKSTEEN, SEAN P. FLANAGAN, FIROZ
JINNAH, INGO W. MUELLER, BRIAN K.
RABINOVITZ, EDWARD JAMES WEXLER,
GARY THOMAS a/k/a GARY THOMAS
VOJTESAK,

Defendants,

and

FLANAGAN & ASSOCIATES, LTD.,

Relief Defendant.

**PLAINTIFF SECURITIES AND EXCHANGE COMMISSION'S RESPONSE TO
DEFENDANT CHAPMAN'S MOTION TO COMPEL RESPONSES TO DISCOVERY**

On August 17, 2009, Defendant Daniel G. Chapman ("Chapman") filed a Motion to
Compel Responses to Discovery Requests ("Motion") (Doc. No. 179) seeking that the Court
order Plaintiff Securities and Exchange Commission ("Commission") to respond to certain of

1 Defendant Chapman's discovery requests. On August 25, 2009, Defendant Sean P. Flanagan
2 ("Flanagan") filed a "Joinder to Daniel G. Chapman's Motion to Compel By Sean P. Flanagan"
3 ("Flanagan Joinder") (Doc. No. 182).¹

4 Given that the Commission has, to date, fully complied with all its discovery obligations,
5 including in responding to Defendant Chapman's discovery requests, the Commission
6 respectfully requests that the Motion be denied. In addition, the Commission hereby respectfully
7 moves for sanctions against Defendants Chapman and Flanagan for: (a) issuance of the discovery
8 requests that are the subject of the Motion and/or (b) filing (or joining in) the Motion. The
9 Commission respectfully requests that it be reimbursed for costs incurred in responding to the
10 Motion. As further discussed below, the discovery requests were issued, and the Motion filed,
11 solely with the goal of harassing and distracting the Commission from the prosecution of this
12 matter.
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14 **PROCEDURAL BACKGROUND**²

15 The Commission filed this action on April 25, 2005 against thirteen defendants alleging
16 they participated in an accounting and stock manipulation scheme related to Exotics.com, Inc., a
17 publicly-traded Nevada corporation, between 1999 and 2002. Specifically, Defendants Chapman
18 and Flanagan are two of eight defendants charged with engaging in (or, alternatively, in aiding
19 and abetting) the manipulation scheme. On September 1, 2005, Defendant Chapman filed a
20 motion to stay this action as a result of unrelated criminal charges then pending against him. On
21 September 13, 2005, Defendant Flanagan joined in Chapman's motion for a stay. The
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24 ¹ Since there are no legal or factual arguments made in the Flanagan Joinder, all
25 arguments herein are directed to the Chapman Motion. However, the Commission respectfully
26 requests that this filing also be treated, and considered, as the opposition to the Flanagan Joinder.

27 ² This background only covers developments related to Defendants Chapman and
28 Flanagan, the movants.

1 Commission opposed Defendants' stay motion. That motion was granted on October 28, 2005.
2 On April 4, 2008, the Commission moved to lift the stay then pending against Defendants
3 Chapman and Flanagan. Defendants Chapman and Flanagan both opposed the Commission's
4 motion. Nonetheless, on May 19, 2008, the Court ruled in favor of the Commission and lifted the
5 stay, effective as of June 16, 2008.
6

7 On June 23, 2008, Defendants Chapman and Flanagan finally responded to the
8 Commission's Complaint by jointly moving that it be dismissed, principally on the ground that it
9 failed to plead fraud with the level of particularity required by Federal Rule of Civil Procedure
10 9(b). The Commission opposed the motion and, after oral argument on August 19, 2008, the
11 Court that same day denied the joint motion to dismiss. On September 15, 2008, Defendants
12 Chapman and Flanagan separately answered the Complaint, denying all of the substantive
13 allegations therein.
14

15 Despite answering the Complaint, on October 17, 2008, Defendants Chapman and
16 Flanagan jointly filed a Notice of Appeal, noting they were taking an appeal to the Court of
17 Appeals for the Ninth Circuit on the denial of their joint motion to dismiss the Complaint. On
18 December 22, 2008, the Commission moved the Ninth Circuit to dismiss the appeal for lack of
19 jurisdiction. On January 21, 2009, the Ninth Circuit – via a one-sentence order – granted the
20 Commission's motion and dismissed the appeal for lack of jurisdiction. On March 13, 2009, the
21 Ninth Circuit issued its mandate giving effect to its January 21st ruling.
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23 On August 3, 2009, Defendant Chapman filed his original Motion to Compel (Doc. 172).
24 On August 5, the Court ordered, *sua sponte*, that the August 3 motion be stricken due to
25 Defendant Chapman's failure to comply with the Federal and local rules of civil procedures'
26 "meet and confer" requirements. (Doc. 174). After a telephone call with undersigned counsel for
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1 the Commission on or about August 13, Defendant Chapman filed the instant (renewed) Motion
2 on August 17 (Doc. No. 179). On August 25, the Flanagan Joinder (Doc. No. 182) was filed.

3 ARGUMENT

4 **I. The Commission Has Produced All Relevant Documents to Defendants**

5 On or about September 11, 2006, pursuant to Fed.R.Civ.P. 26(a)(1), the Commission
6 served upon all defendants, including Defendants Chapman and Flanagan, its Initial Disclosures.
7 See Exhibit A (attaching Initial Disclosures). The Initial Disclosures disclosed thirty-three
8 individuals then known to the Commission “likely to have discoverable information relevant to
9 the disputed facts alleged in the Complaint.” The Initial Disclosures also noted that “[v]ia letter
10 dated April 19, 2006, the Commission has previously produced to all of the defendants copies of
11 all the transcripts containing the investigative testimony” of the thirty-three individuals and of all
12 the individual defendants.
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14 In addition, the Initial Disclosures listed ninety “sources of all non-privileged documents
15 contained in the Commission’s files of the investigation giving rise to this action.” The Initial
16 Disclosures also noted that, via the April 19 letter, “the Commission has previously produced to
17 all of the defendants all of the documents” produced by the ninety sources. Finally, the Initial
18 Disclosures noted that, in addition to the ninety sources, there were four additional categories of
19 documents in the Commission’s files and that “[t]hese additional documents may be viewed at
20 any reasonable time at the Commission’s Boston ... Office.” The four additional categories of
21 documents included copies of the following: correspondence; subpoenas; Wells Submissions;
22 and a copy of the Formal Order of Investigation.
23

24 On or about March 3, 2009, via a letter from attorney Rachel E. Hershfang to Defendants
25 Chapman and Flanagan, the Commission produced to them “a disk containing copies of
26 documents seized by the Internal Revenue Service during the search of your offices.” Ms.
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1 Hershfang noted in the March 3 letter that the information on the disk “was provided to the SEC
2 by the IRS during the criminal investigation in your case” and that “[g]iven the conclusion of the
3 [criminal] case, the IRS recently gave us permission to provide a copy to you.” Ms. Hershfang
4 also noted that “[b]ecause there may be privileged material on the disk, I wanted to provide it to
5 you and determine collectively how best to proceed.” See Exhibit 8 to Defendant Chapman’s
6 Memorandum of Points and Authorities (“Chapman Memorandum”) (attaching copy of 3/3/09
7 letter).

9 On July 29, 2009, undersigned counsel sent an email to all remaining defendants,
10 including Defendants Chapman and Flanagan, noting the Commission’s intention to shortly
11 circulate a supplemental Rule 26(a) disclosure with the names of at least two individuals (Robert
12 Potter and Shawn Hackman) who may have information related to this matter. See Exhibit B
13 (copy of 7/29/09 email). On August 5, 2009, attorney David H. London sent a second email to all
14 remaining defendants, including Defendants Chapman and Flanagan, noting that the Commission
15 intended to name at least one additional individual (David Martin of the British Columbia
16 Securities Commission) in its anticipated supplemental Rule 26(a) disclosure. See Exhibit C
17 (copy of 8/5/09 email). On August 11, 2009, undersigned counsel sent the Commission’s
18 Supplemental Disclosures (previously referenced in the July 29 and August 5 emails) to all
19 remaining defendants, including Defendants Chapman and Flanagan. See Exhibit D (copy of
20 8/11/09 Supplemental Disclosures).

23 *With one exception* – further discussed below – the Commission has produced, or made
24 available, to all of the defendants remaining in this action (including Defendants Chapman and
25 Flanagan) all documents it “may use to support its claims.” Fed.R.Civ.P. 26(a)(1)(A)(ii). In
26 addition, the Commission has provided to all remaining defendants (including Defendants
27 Chapman and Flanagan) the names and contact information of “each individual likely to have
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1 discoverable information.” Fed.R.Civ.P. 26(a)(1)(A)(i). Moreover, as discussed above, the
2 Commission has periodically supplemented its disclosures as required by Fed.R.Civ.P. 26(e).

3 The Commission has also made available to defendants (including Defendants Chapman
4 and Flanagan) copies of transcripts of each individual who testified before its staff during the
5 private investigation. Moreover, the Commission staff has, thus far, deposed nearly twenty
6 individuals during discovery. All defendants (including Defendants Chapman and Flanagan)
7 have, of course, had the opportunity to attend and participate in these depositions.
8

9 The *one exception* related to documents that the Commission *may use to support its*
10 *claims* (or which may lead to the discovery of admissible evidence) that it has not yet produced to
11 defendants (including Defendants Chapman and Flanagan) has been some of the documents it
12 received from the British Columbia Securities Commission (BCSC). These are the documents
13 that were seized by the BCSC from the offices of St. George Capital, a Vancouver-based entity
14 affiliated during the relevant period with at least two of the defendants (Ingo W. Mueller and
15 Firoz Jinnah). As the Court may recall, there has been an attorney-client privilege issue with
16 respect to such documents. As undersigned counsel for the Commission noted during the last
17 status conference (held on August 13, 2009), once the privilege issue is resolved, it is the
18 Commission staff’s intention to produce the BCSC-seized documents to all defendants, including
19 Defendants Chapman and Flanagan.
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22 In sum, *with a single exception (explained above)*, the Commission has either produced,
23 or made available, to Defendants Chapman and Flanagan *every single document that it intends to*
24 *use in support of its claims*. In addition, the Commission has informed Defendants Chapman and
25 Flanagan about *every single individual that it is aware of who may have discoverable*
26 *information*. Moreover, the Commission has produced to Defendants Chapman and Flanagan
27 *every single transcript created during the course of the Commission’s investigation*. In light of
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1 these facts, there can be no doubt but that Defendant Chapman's discovery requests – the subject
2 of the Motion – have been issued with a single goal in mind: to attempt to harass and distract the
3 Commission from the litigation of this matter.

4
5 **II. The Appropriateness of Communications With Other Law Enforcement**
6 **Agencies**

7 One of Defendant Chapman's principal contentions is that he is legally entitled to all
8 information about, and documents reflecting, communications between the Commission (or its
9 staff) and other law enforcement agencies.³ The Chapman Memorandum devotes approximately
10 three pages to a sub-section entitled "Relevance of Communications With the United States
11 Attorney's Office." In that sub-section, Defendant Chapman makes the rather pedestrian
12 observation "that the Office of the United States Attorney for the District of Nevada is and has
13 been working with Plaintiff on this case." Chapman Memorandum, p.5. Defendant Chapman
14 then proceeds, for the next several pages, to outline all the tell-tale signs supporting his "belief"
15 that the Commission is, or has been, working with the U.S. Attorney's Office. See id., pp.5-7.
16 Defendant Chapman then concludes that the information and documents he seeks are relevant
17 because "the allegation that the United States Attorney's Office is the driving force behind this
18 case and will be a major part of Mr. Chapman's defense." Id., p.7.

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21 ³ See Chapman Memorandum, p.4 (noting that the Commission has refused to answer
22 Interrogatories No.7 and No. 8 which collectively seek information about the Commission's (and
23 its staff's) communications related to Defendant Chapman with third parties, including, but not
24 limited to, other law enforcement agencies such as the Department of Justice and the U.S.
25 Attorney's Office for the District of Nevada). See also related Requests for Production No. 7 and
26 No. 8 in Defendant Daniel G. Chapman's First Set of Requests for Production of Documents to
27 Plaintiff Securities and Exchange Commission ("Chapman Interrogatories"), attached as Exhibit 3
28 to Chapman Memorandum. The Commission also objected (and continues to object) to
Interrogatory No. 17 on the ground that it is "an impermissible attempt to expand the number of
allowed interrogatories beyond the number allowed by Fed.R.Civ.P. 33." Exhibit 5 to Chapman
Memorandum.

1 Firstly, the Commission has never denied that its staff has had numerous communications
2 over the years with a number of law enforcement agencies that have either investigated and/or
3 prosecuted some of the defendants in this action – including the U.S. Department of Justice
4 (DOJ), the Internal Revenue Service (IRS) and the British Columbia Securities Commission
5 (BCSC). For example, during the Commission’s investigation, the staff provided Defendants
6 Chapman and Flanagan (as it does with all witnesses that appear before it) with a Commission
7 Form 1662. See Exhibit E (excerpts from investigative testimonies of Defendants Chapman and
8 Flanagan). Form 1662 contains certain warnings, including that “[t]he Commission often makes
9 its files available to other governmental agencies, particularly the United States Attorneys and
10 state prosecutors. There is a likelihood that information supplied by you will be made available
11 to such agencies where appropriate.” United States v. Stringer, 535 F.3d 929, 934 (9th Cir. 2008)
12 (quoting Form 1662) (internal quotations omitted). In addition, the staff warned Defendants
13 Chapman and Flanagan during their testimonies (as it does with all witnesses that appear before
14 it) that “the facts developed in this investigation might constitute violations of ... Federal or state
15 ... criminal laws.” See Exhibit E.

16 Secondly, the Form 1662 provided to Defendants Chapman and Flanagan during the
17 investigation expressly noted that they (like all other witnesses subpoenaed to testify before the
18 staff), could assert their Fifth Amendment rights. As the Court of Appeals for the Ninth Circuit
19 noted in Stringer: “After the heading ‘Fifth Amendment and Voluntary Testimony,’ the form
20 states that:
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24 Information you give may be used against you in any federal ... civil or
25 criminal proceeding brought by the Commission [or] any other agency.
26 You may refuse, in accordance with the rights guaranteed to you by the
27 Fifth Amendment of the Constitution of the United States, to give any
28 information that may tend to incriminate you or subject you to fine,
penalty, or forfeiture.

1 Id. at 934-35. In fact, Defendants Chapman and Flanagan both invoked their Fifth Amendment
2 rights during investigative testimony before the Commission staff. See Complaint, ¶¶ 13-14.
3 However, despite the warnings in Form 1662, Defendant Chapman and the law firm of Flanagan
4 & Associates⁴ provided documents to the staff during the investigation. See Exhibit A (Exhibit B
5 to Initial Disclosures). As such, Defendants Chapman and Flanagan cannot now complain about
6 the Commission staff's provision of documents and/or information received from them (or from
7 any other witness who appeared before the staff during its investigation) to the DOJ. See
8 Chapman Memorandum, pp.5-6.

10 Lastly, after the Commission investigation ended and the Complaint in this matter was
11 filed, the staff did not hide the fact that it had communicated, and continued communicating, with
12 other law enforcement agencies. For example, in a privilege log provided by the staff to
13 Defendant Chapman in February 2009, the staff noted that it had documents in its files reflecting
14 communications with the IRS and the Bermuda Monetary Authority. See Exhibit 7 to Chapman
15 Memorandum (attaching a copy of the privilege log). Similarly, in the March 3, 2009 letter from
16 Commission attorney Hershfang to Defendants Chapman and Flanagan, the staff referenced a
17 recent communication it had had with the IRS. See Exhibit 8 to Chapman Memorandum
18 (attaching copy of 3/3/09 letter). The staff has also throughout let it be known that it has had in
19 its possession a voluminous amount of documents seized by the BCSC from the offices of St.
20 George Capital in Vancouver, Canada.

23 The Supreme Court, the Court of Appeals for the Ninth Circuit and other courts have all
24 made clear that it is completely appropriate for the Commission staff to coordinate its
25 investigations, and share information derived therefrom, with other law enforcement agencies,
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27 ⁴ An apparent successor to the law firm of Chapman and Flanagan.
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1 including the DOJ. See United States v. Stringer, 535 F.3d at 936-37 (“The Supreme Court has
 2 held that the government may conduct parallel civil and criminal investigations without violating
 3 the due process clause, so long as it does not act in bad faith.”) (citing United States v. Kordel,
 4 397 U.S. 1, 11 (1970)); *id.* at 933 (“Federal securities laws authorize the SEC to transmit
 5 evidence it has gathered to the USAO to facilitate a criminal investigation by the USAO.”) (citing
 6 15 U.S.C. §§ 77t(b), 78u(d)).⁵ Thus, Defendants’ complaint about the Commission staff’s
 7 provision of information to another law enforcement agency is completely unfounded.

9 **III. The Commission and Its Staff Have Never Acted in Bad Faith**

10 In Stringer, the Ninth Circuit held that Commission staff members had *not* acted
 11 inappropriately (or in “bad faith”) even though:

12 [t]he SEC facilitated the criminal investigation in a number of ways. The
 13 SEC offered to conduct the interviews of defendants so as to create ‘the
 14 best record possible’ in support of ‘false statement cases’ against them,
 15 and the AUSA instructed the SEC Staff Attorney on how best to do that.
 16 The AUSA asked the relevant SEC office, based in Los Angeles, to take
 17 the depositions in Oregon so that the Portland Office of the USAO would
 have venue over any false statements case that might arise from the
 depositions, and the SEC did so.

18 535 F.3d at 934; see also Dresser, 628 F.2d at 1385-86 (Congress has “acknowledged the SEC’s
 19 dual investigative role in preparing cases for civil and criminal enforcement actions. [It] also
 20 recognize[s] the necessity of close cooperation between the SEC and Justice in preparing such
 21 cases.”).

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 24 ⁵ See also SEC v. Dresser Industries, Inc., 628 F.2d 1368, 1376 (D.C. Cir. 1980) (en
 25 banc) (the federal securities laws “explicitly empower the SEC to investigate possible infractions
 26 of the securities laws with a view to both civil and criminal enforcement, and to transmit the fruits
 27 of its investigations to Justice in the event of potential criminal proceedings.”); cf. Standard
 28 Sanitary Manufacturing Co. v. United States, 226 U.S. 20, 52 (1912) (“The Sherman Act provides
 for a criminal proceeding to punish violations and suits in equity to restrain such violations, and
 the suits may be brought simultaneously or successively. The order of their bringing must depend
 upon the Government ...”).

1 In the context of parallel investigations and prosecutions, the Supreme Court and Ninth
2 Circuit have declared that “the government may act in bad faith if it brings a civil action *solely* for
3 the purpose of obtaining evidence in a criminal prosecution and does not advise the defendant of
4 the planned use of evidence in a criminal proceeding.” Stringer, 535 F.3d at 937 (emphasis
5 added) (citing Kordel, 397 U.S. at 12-13); id. at 937 (“District courts have occasionally
6 suppressed evidence or dismissed indictments on due process grounds where the government
7 made affirmative misrepresentations or conducted a civil investigation *solely* for purposes of
8 advancing a criminal case.”) (emphasis added) (citations omitted).

10 In this case, Defendants Chapman and Flanagan have not pointed to any evidence (or
11 facts) suggesting any “bad faith” on the Commission’s (or its staff’s) part. As summarized above,
12 during the investigation, the Commission staff provided Forms 1662 to both Defendants. The
13 Form 1662 expressly informed Defendants Chapman and Flanagan about their Fifth Amendment
14 rights and that there was “a likelihood that information supplied by you will be made available”
15 to criminal prosecutors. Defendants Chapman and Flanagan (as practicing attorneys) clearly
16 understood those warnings – as evidenced by the fact that they both selectively asserted their
17 Fifth Amendment rights during the investigation (i.e., asserting the Fifth during testimony but not
18 with respect to certain documents produced to the staff).

20 In addition, Defendants Chapman and Flanagan cannot seriously contend (and certainly
21 cannot point to any evidence suggesting) that the Commission decided to investigate them, and
22 then file a civil action against them, “solely for the purpose of obtaining evidence” to be used in
23 their criminal prosecution. As recognized in the Chapman Memorandum, see p.2, the
24 Commission issued its Formal Order of Investigation related to the Exotics matter on January 15,
25 2002. Defendants Chapman and Flanagan were criminally charged in August 2003 for conduct
26 *unrelated* to Exotics – the company that is the subject of this proceeding. The Commission then
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1 filed this Exotics-related action in April 2005. Thus, on its face, it is clear that the Commission
 2 had its own independent reasons for investigating and charging Defendants Chapman and
 3 Flanagan. See Stringer, 535 F.3d at 939 (there was no bad faith on the Commission's part where,
 4 among other things, its investigation "was not a pretext for the USAO's criminal investigation of
 5 defendants."); id. at 939 (there was no bad faith by the U.S. Department of the Treasury where it
 6 "instituted its investigation before any indictment and in order to file its own civil complaint.")
 7 (citing United States v. Unruh, 855 F.2d 163, 1374 (9th Cir. 1987)).⁶

9 Moreover, there simply would not have been any reason for the DOJ to use the
 10 Commission staff to obtain whatever evidence or information it needed to build (or attempt to
 11 build) its criminal case against Defendants Chapman and Flanagan. Not only did the DOJ have
 12 access to (and obtain evidence from) other investigative agencies – such as the IRS personnel
 13 who worked on the criminal prosecution – but it also presumably could have obtained whatever
 14 evidence it needed against Defendants Chapman and Flanagan via Grand Jury subpoenas. See
 15 Dresser, 628 F.2d at 1381 ("the subpoena power of the grand jury is as broad [or] perhaps broader
 16 than that of the SEC. Justice can procure from [defendant] directly whatever materials it might
 17 procure indirectly through the SEC.").

19 In short, there is no evidence (or facts) suggesting that the DOJ is the "driving force
 20 behind this case," as claimed in the Chapman Memorandum, p.7. To the contrary, the evidence is
 21 that the Commission investigated, and charged, Defendants Chapman and Flanagan for its own
 22 purposes – i.e., to enforce alleged violations of the federal securities laws with respect to Exotics,
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24 ⁶ See also Dresser, 628 F.2d at 1387 ("Where the [Commission] has a legitimate
 25 noncriminal purpose for the investigation, it acts in good faith ... even if it might use the
 26 information gained in the investigation for criminal enforcement purposes as well."); id. at 1388
 27 ("Nor does the participation of two SEC attorneys in the Justice task force cast doubt upon the
 28 good faith of the Commission."); United States v. Churchill, 483 F.2d 268, 272 (1st Cir. 1973);
United States v. Teyibo, 877 F. Supp. 846, 855 (S.D.N.Y. 1995).

1 a company that was not even the subject of the criminal charges filed against them.⁷ As such,
 2 Defendants are not entitled to discovery on the substance of any communications between the
 3 Commission (or its staff) and other law enforcement agencies. See Dresser, 628 F.2d at 1388
 4 (defendant in Commission subpoena enforcement action not allowed discovery on, among other
 5 things, “the SEC criminal referral” and “the ethical propriety of SEC agents’ participation in the
 6 criminal investigation.”); id. at 1388 (“Discovery should be permitted only where the [defendant]
 7 is able to distinguish himself from ‘the class of the ordinary [defendant],’ ... by citing special
 8 circumstances that raise doubts about the agency’s good faith.”) (citations omitted); id. at 1388-89
 9 (defendant “has suggested no improper motive for the SEC investigation” and his “bare
 10 protestations of innocence do not suffice to call the SEC’s bona fides into question.”).

11 **IV. Communications Between Commission Staff and Other Law Enforcement** 12 **Agencies Are Privileged**

13 In response to Defendant Chapman’s discovery requests (the subject of the Motion), the
 14 Commission lodged both general and specific objections to any discovery request that sought to
 15 probe into the substance of communications between the Commission (or its staff) and other law
 16 enforcement agencies. See Exhibits 4-6 to Chapman Memorandum (Commission responses to
 17 Defendant Chapman’s discovery requests). The Commission refused to respond to such
 18 discovery requests on the ground that communications between it (or its staff) and other law
 19 enforcement agencies are not discoverable given the “work-product immunity, law enforcement
 20 privilege [and] deliberative privilege.” Exhibit 5 to Chapman Memorandum, p.2, ¶ 2 (general
 21 objections to interrogatories); pp.10-11 (specific responses to Interrogatories No. 7 and 8);
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 26 ⁷ This is not to in any way suggest, of course, that it is inappropriate for the Commission
 27 and the DOJ to bring simultaneous civil and criminal charges against the same defendant for the
 28 same underlying conduct. That is a commonplace occurrence.

1 Exhibit 6 to Chapman Memorandum, p.2, ¶ 2 (general objections to request for production of
2 documents); pp.5-6 (specific responses to Requests for Production No. 7 and 8).

3 In addition, in response to an inquiry by Defendant Chapman, the Commission reasserted
4 its position on the matter (i.e., that such communications are privileged) in a December 8, 2008
5 letter from Commission attorney Hershfang to Defendant Chapman that cited legal authority for
6 the Commission's position. See Exhibit F (copy of 12/8/08 letter).⁸ That should have, of course,
7 been the end of Defendant Chapman's (and now Defendant Flanagan's) efforts to inquire into
8 such communications. Instead, they have pressed on for the substance of such communications
9 via the Motion – supported by the Chapman Memorandum, a document drafted by a practicing
10 attorney that yet does not cite a single source of law for any of its proffered legal propositions.
11

12 “The Federal Rules of Civil Procedure contemplate broad discovery, permitting discovery
13 ‘regarding any matter, *not privileged*, which is relevant to the subject matter involved in the
14 pending action.’” United States v. Farley, 11 F.3d 1385, 1390 (7th Cir. 1993) (emphasis in
15 original) (quoting Fed.R.Civ.P. 26(b)(1)). Communications between the Commission (or its
16 staff) and other law enforcement agencies are protected from discovery by the deliberative
17 process privilege and/or the work product doctrine.
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19 “The deliberative process privilege protects communications that are part of the decision-
20 making process of a governmental agency. ... Since frank discussion of legal and policy matters
21 is essential to the decisionmaking process of a governmental agency, communications made prior
22 to and as part of an agency determination are protected from disclosure.” Farley, 11 F.3d at 1389
23 (citing NLRB v. Sears, Roebuck & Co., 421 U.S. 132, 150-152 (1975)). “The deliberative
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26 ⁸ Ms. Hershfang's letter only addressed the deliberative and law-enforcement privileges
27 (and not the work-product doctrine) since it was attempting to address specific questions that had
28 been posed by Defendant Chapman to undersigned counsel.

1 process privilege may be overcome where there is a sufficient showing of a particularized need to
2 outweigh the reasons for confidentiality.” *Id.* (citing Coastal States Gas Corp. v. Dep’t of Energy,
3 617 F.2d 854, 868 (D.C. Cir. 1980); Black v. Sheraton Corp. of America, 564 F.2d 531, 545
4 (D.C. Cir. 1977)). “[R]elevance alone is an insufficient reason for breaching the deliberative
5 process privilege.” *Id.* at 1390.

7 One of the documents sought during discovery by the civil defendant in Farley was “the
8 referral memorandum from the FTC [Federal Trade Commission] staff to the Department of
9 Justice.” 11 F.3d at 1389. The court refused to order production of the document because
10 “[h]aving been rendered prior to the Department’s decision to bring an action against [defendant],
11 the document is within the Department’s deliberative process privilege. Since the document was
12 pre-decisional and deliberative, *the fact that the document passed from one agency to another*
13 *does not terminate its privileged status.*” *Id.* (emphasis added) (citing Renegotiation Board v.
14 Grumman Aircraft Engineering Corp., 421 U.S. 168 (1975); Bureau of Nat’l Affairs, Inc. v.
15 United States Dep’t of Justice, 742 F.2d 1484 (D.C. Cir. 1984)).

17 Similarly, in FDIC v. Eagle Properties, 105 F.R.D. 12, 15; 1984 U.S. Dist. LEXIS 21665
18 (D.C. 1984), a party sought discovery from the Commission of, among other things,
19 “communications between SEC and OCC [Office of the Comptroller of the Currency] staff.” The
20 court noted: “The deliberative process privilege protects from disclosure those communications
21 within the federal government which consist of advice, recommendations, opinions, and other
22 information transfers involved in the deliberative processes of governmental agencies.” *Id.*
23 (citing Murphy v. Department of the Army, 613 F.2d 1151, 1154 (D.C. Cir. 1979); Brinton v.
24 Dep’t of State, 636 F.2d 600 (D.C. Cir. 1980); McClelland v. Andrus, 606 F.2d 1278, 1287-88
25 (D.C. Cir. 1979)). The court noted that: “For the privilege to apply, the communication or
26 document must have been predecisional and must have been deliberative in that it was actually
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1 related to the decision making process.” Id. (citing Kansas State Network, Inc. v. FCC, 720 F.2d
2 185, 191 (D.C. Cir. 1983); Jordan v. Dep’t of Justice, 591 F.2d 753, 772-79 (D.C. Cir. 1978) (en
3 banc)).

4 The Eagle Properties court concluded that the information sought from the Commission
5 was protected from discovery by the deliberative process privilege. It noted that:

7 The information sought comes from communications between SEC and
8 OCC staff which took place during the course of the two agencies’
9 investigations These communications concerned litigation strategy
10 generally, and such specific topics as what issues were raised in the case,
11 what witnesses to call for deposition, and what questions should be asked.
12 Most notably, the communications involved staff discussions of the
13 preparation and filing of the action against [defendant] and the allegations
14 to be made in the complaint ... These communications and documents are
clearly protected by the deliberative process privilege. First, they are
predecisional in that they all relate to, and precede, the final decision to
file an action against [defendant]. Further, they are clearly deliberative in
that they were an integral part of the formulation of decisions throughout
the investigations and the eventual filing of the lawsuit.

15 Id.

16 In addition, the Eagle Properties court separately concluded that the information sought
17 from the Commission was protected from discovery by the work-product doctrine, which
18 “shelters the mental processes of the attorney, [providing] a privileged area within which he can
19 analyze and prepare his client’s case. ... This doctrine has been codified in Fed.R.Civ.P. 26.”

20 Id. at 15-16 (internal quotations omitted) (citing United States v. Nobles, 422 U.S. 225, 238
21 (1975); Hickman v. Taylor, 329 U.S. 495 (1947)). The court noted that “[i]n order to obtain
22 [work-product] materials, the defendant/movant must show a substantial need,” something
23 defendant/movant had not shown. Id. at 16 (citing Fed.R.Civ.P 26; Hickman, 329 U.S. at 512).
24 See also Farley, 11 F.3d at 1390 (“Documents protected by the work product privilege ... need
25 only be disclosed upon a showing of substantial need.”).
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1 Finally, the communications sought by Defendants Chapman and Flanagan are also
 2 protected by the law-enforcement privilege. See Commonwealth of Puerto Rico v. United
 3 States, 490 F.3d 50, 61-65 (1st Cir. 2007); see also Roviato v. United States, 353 U.S. 53, 59
 4 (1957); In re U.S. Dep't of Homeland Sec., 459 F.3d 565 (5th Cir. 2006); In re Dep't of
 5 Investigation of the City of New York, 856 F.2d 481, 484 (2d Cir. 1988) ("The purpose of this
 6 privilege is to prevent disclosure of law enforcement techniques and procedures, to preserve the
 7 confidentiality of sources, to protect witness and law enforcement personnel, to safeguard the
 8 privacy of individuals involved in an investigation, and otherwise to prevent interference with an
 9 investigation."); Black v. Sheraton Corp. of Am., 564 F.2d 531, 545 (D.C. Cir. 1977) (public has
 10 an interest in "minimizing disclosure of documents that would tend to reveal law enforcement
 11 investigative techniques or sources."). The law enforcement privilege can only be overcome "by
 12 a sufficient showing of need." Commonwealth of Puerto Rico, 490 F.3d at 62.

15 For the reasons discussed above, it is clear that communications between the Commission
 16 (or its staff) and other law enforcement agencies are protected from discovery by the deliberative
 17 process and/or law enforcement privileges and/or the work-product doctrine. Defendants have
 18 not shown (or suggested) any "particularized need" to overcome the deliberative process
 19 privilege, see Farley, 11 F.3d at 1389; nor a "sufficient" need to overcome the law enforcement
 20 privilege, see Commonwealth of Puerto Rico, 490 F.3d at 62; nor a "substantial need" to
 21 overcome the work product doctrine, see Eagle Properties, 105 F.R.D. at 16; Farley, 11 F.3d at
 22 1390. Nor have they shown (or suggested) any bad faith (or lack of good faith) on the part of the
 23 Commission or its staff necessitating discovery of such communications.

25 **V. Communications Between Commission Staff and Other Law Enforcement**
 26 **Agencies Are Also Here Not Relevant**

27 As the Farley and Eagle Properties courts also noted, it is difficult, if not impossible, for a
 28 movant to show a "particularized" or "substantial" need for privileged documents when they are

1 irrelevant to the matter before the court. As the Farley court put it: "Since the documents at issue
2 are not relevant to the controversy before us, [defendant] cannot, as a matter of law, make a
3 showing of need." 11 F.3d at 1390. Similarly, the Eagle Properties court concluded that "[n]ot
4 only are the SEC materials privileged, but the Court cannot see any way in which they could be
5 relevant to the ... transaction at issue in this case." 105 F.R.D. at 16.
6

7 Likewise, Defendants Chapman and Flanagan have failed to show how the underlying
8 contents of communications between the Commission or its staff and other law enforcement
9 agencies could possibly be relevant to determining the truthfulness (or not) of the allegations in
10 the Complaint. See Farley, 11 F.3d at 1390 ("The discovery proposed here is not relevant to the
11 issue presented by the government's complaint."). It is also not clear how the contents of such
12 communications could possibly aid Defendants in defending against the Commission's
13 allegations since nowhere in their Answers do they assert misconduct by either the Commission
14 or the criminal authorities as an affirmative defense. (Docs. No. 133 (Flanagan) and 134
15 (Chapman)). See Farley, 11 F.3d at 1390 ("Nor is the proposed discovery relevant to any of
16 [defendant's] affirmative defenses.").

17
18 As discussed above, with a limited exception, the Commission staff has already produced
19 to all of the remaining defendants in this matter every document it may seek to introduce at trial
20 in support of its claims. It has also made available to all defendants the names (and, where
21 available, the contact information) of all individuals who may have any information relevant to
22 the claims and allegations in the Complaint. That is the sort of relevant information that might
23 aid Defendants Chapman and Flanagan in defending against the Complaint. On the contrary,
24 communications between the Commission or its staff and other law enforcement agencies are
25 simply not relevant to determining the merits of the Complaint or of any (legitimate) defense
26 thereto. See Farley, 11 F.3d at 1390-91 ("The suppositions of FTC staff members expressed in
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1 internal memoranda,” “intra-agency communications,” and “the postulations of agency staff
2 members” are not relevant to the matter before the court).

3 **VI. The Discovery Requests Are Unduly Burdensome and Intended to Harass**

4 As the Commission noted in response to the discovery requests that are the subject of the
5 Motion, the requests are “unduly burdensome, unreasonable and intended to harass.” See Exhibit
6 5 to Chapman Memorandum, p.3, ¶ 5 (general objections to interrogatories). As admitted in the
7 Chapman Memorandum, many of the interrogatories and document requests purport to require the
8 Commission to identify “all of the evidence” it might “intend to rely at trial to support” an
9 allegation made in the Complaint. See Chapman Memorandum, pp.3-5; see also Exhibits 2 and 3
10 to Chapman Memorandum (respectively, the interrogatories and document requests).

11
12 In other words, with the Motion, Defendants Chapman and Flanagan seek the Court to
13 compel the Commission to cull through thousands of pages of investigative and deposition
14 transcripts and other documents and to specifically identify every piece of evidence that it intends
15 to introduce at trial in support of specific allegations made in the Complaint. As noted above,
16 these thousands of pages of documents have already been provided to Defendants Chapman and
17 Flanagan. They are able themselves (especially as attorneys) to review them and determine what
18 evidence the Commission is likely to seek to introduce against them at the trial of this matter.
19 They are not entitled to obtain from the Commission during discovery what amounts to an outline
20 of an opening or closing statement. Not surprisingly, the Chapman Memorandum does not cite
21 any case law in support of the imposition of such an unduly burdensome task on the Commission.
22 In fact, the Chapman Memorandum does not cite a single case in support of any of the purported
23 legal propositions it advances.

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26 Clearly, what Defendants Chapman and Flanagan seek via the Motion and the Chapman
27 Memorandum is to re-litigate the motions to dismiss which they filed and lost. See Chapman
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1 Memorandum, p.9 (re-arguing that “FRCP 9(b) requires that a complaint alleging fraud requires
2 pleading with specific particularity” and “that the SEC has not met their obligations under FRCP
3 9(b) and is simply conducting a fishing expedition.”). With the discovery requests here at issue,
4 Defendants simply seek a greater level of pleading detail than required by Fed.R.Civ.P. 9(b) – a
5 matter that has already been decided by the Court.
6

7 Finally, as discussed above, the discovery requests clearly seek privileged and/or
8 protected material and the Defendants have not shown any type of need whatsoever for the
9 materials. As such, the requests are clearly unduly burdensome, unreasonable and intended to
10 harass.

11 **VII. Sanctions Should Here Be Imposed**

12 As attorneys, Defendants Chapman and Flanagan know (or must be presumed to know)
13 that there is no legal support whatsoever for obtaining the information they seek from the
14 Commission. Most of the information they seek is, as detailed above, clearly privileged and/or
15 protected from discovery. Moreover, they have not even attempted to make (nor could they
16 make) any type of a showing of “need” for such information – since the information they seek is
17 irrelevant to these proceedings. Especially in light of the fact that, with a limited exception, the
18 Commission has turned over its entire investigative file (and the names of all relevant individuals)
19 to Defendants Chapman and Flanagan, there can be no doubt that the Motion is frivolous and that
20 the related discovery requests are clearly burdensome, unreasonable and intended to harass. See
21 Fed.R.Civ.P. 26(g)(1)(B) (discovery request must, *inter alia*, be “consistent with these rules and
22 warranted by existing law or by a nonfrivolous argument for extending, modifying, or reversing
23 existing law, or for establishing new law” and must not be “interposed for any improper purpose,
24 such as to harass”); Advisory Committee Notes to 1983 Amendment to Fed.R.Civ.P. 26
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1 (“Advisory Notes”) (“[E]very discovery request ... should be grounded on a theory that is
2 reasonable under the precedents or a good faith belief as to what should be the law.”).

3 Given the Motion’s frivolity, sanctions are here appropriate. See Fed.R.Civ.P.
4 26(g)(1)(B) (if discovery request violates rules of civil procedure, “the court, on motion or on its
5 own, *must* impose an appropriate sanction ...”) (emphasis added); Advisory Notes (“The new
6 rule *mandates* that sanctions be imposed on attorneys who fail to meet the standards established
7 [therein].”). The Court should, at a minimum, order Defendants Chapman and Flanagan “to pay
8 the reasonable expenses, including attorney’s fees, caused by the[ir] violation.” Fed.R.Civ.P.
9 26(g)(1)(B).
10

11 CONCLUSION

12 For the reasons discussed above, the Commission respectfully requests that the Motion be
13 denied and, for the reasons discussed herein, that sanctions be imposed against Defendants
14 Chapman and Flanagan.
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20 September 4, 2009

Respectfully submitted,

21 /s/ Silvestre A. Fontes
22 Silvestre A. Fontes
23 Thomas J. Rappaport
24 David H. London
25 SECURITIES & EXCHANGE COMMISSION
26 33 Arch Street, 23rd Floor
27 Boston, MA 02110-1424
28 (617) 573-8991 (Fontes)
(617) 573-5940 (fax)
fontess@sec.gov

CERTIFICATE OF SERVICE

I, Silvestre Fontes, hereby certify that on September 4, 2009 I caused copies of the Securities and Exchange Commission's Opposition to Defendants Chapman's Motion to Compel to be served via first-class U.S. mail, upon the following persons:

O. Robert Meredith, Esq
1111 Brickyard Road Suite 206
Salt Lake City, UT 84106-2597
robert@meredithlaw.com
(counsel for defendant Andersen)

Kelly O. Slade, Esquire
Law Offices of Kelly Slade, Ltd
3340 Camino Gardens Way
Las Vegas, NV 89146
kslade@embarqmail.com
(local counsel for defendant Andersen)

David A. Zisser, Esquire
Isaacson Rosenbaum P.C.
633 17th Street Suite 2200
Denver, CO 80202-3622
dzisser@ir-law.com
(counsel for Jinnah and Mueller)

Thomas W. Davis, II
Howard & Howard
3800 Howard Hughes Pkwy Suite 1400
Las Vegas, NV 89169
(local counsel for Jinnah and Mueller)
TDavis@howardandhoward.com

Daniel G. Chapman, Esquire
1235 N. Clybourn Suite A-187
Chicago, IL 60610
DGChap@cox.net
(Pro Se)

Donald J. Christie, Esquire
7143 Mission Hills Dr.
Las Vegas, NV 89113
donchristie@aol.com
(counsel for defendant Corso)

Sean T. Prosser, Esquire
Tyson E. Marshall, Esquire
Morrison & Foerster LLP
12531 High Bluff Drive, Suite 100
San Diego, CA 92130-2040
sprosser@mofo.com
tmarshall@mofo.com
(counsel for Rabinovitz and Brinsky)

David J. Merrill, Esquire
David J. Merrill, P.C.
2850 West Horizon Ridge Pkwy # 200
Henderson, NV 89052
(local counsel for Rabinovitz and Brinsky)

Sean Flanagan and Flanagan & Associates, Ltd
Flanagan Ltd.
7251 W. Lake Mead Blvd Suite 300
Las Vegas, NV 89128
grumpysean@yahoo.com
(Pro Se)

James L. Ericksteen
1228 West Hastings St. # 1502
Vancouver, B.C. V6E 4S6
CANADA
jericksteen@yahoo.ca